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CASE NO: _____

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1984

DONALD N. LLOYD AND JESSICA LLOYD,

PETITIONERS

Versus

PROFESSIONAL REALTY SERVICES, INC.,

RAIFORD ELLIS, JAMES O. RICHARDS,

LOURAINE D. BERRY, ALLAN W. HOOPER, JR.

AND RICHARD SIDWELL, RESPONDENTS

ON WRIT OF CERTIORARI

TO THE UNITED STATES COURT OF APPEALS

FOR THE ELEVENTH CIRCUIT

PETITION FOR CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether knowledge or reason to know that a sale of securities violated the Uniform Securities Act, bars the purchaser from his right to rescission under the Act.

2. Whether offers to shareholders and offers to others, either of which might be exempt alone, must be considered together or separately in determining whether they are exempt from registration under the Uniform Securities Act - i.e., whether the offeror can "stack" or "cumulate" exempt offers, or whether they must be "integrated" and considered as one.

3. Whether the following evidence raises a jury question, whether a corporation's liabilities exceeded its assets at a fair valuation:

a. Thirty-six internally prepared balance sheets and income statements showing liabilities in excess of asset book value, and losses for every month to date;

b. An admission during discovery that at all times the corporation's liabilities exceeded the "book value" of its assets; and

c. An admission during discovery, amended by the Court of Appeals *sua sponte*, that at all times the corporation's liabilities exceeded the "value" of its assets.

4. Whether in a Uniform Securities Act rescission suit the testimony of some of the defendants, bearing the burden of proof that a securities offering was exempt as made to 10 or fewer, that they did not themselves make more than 9 offers or know of any other offers, is

sufficient to remove the issue as a jury question.

5. Whether a secretary's drafts of minutes of a meeting of a board of directors, regularly made at such meetings and kept in the corporate files, or her testimony, both showing that the officers and directors admitted offers and sales of securities to more than ten persons, are admissible under the following hearsay exceptions:

(a) as "business records" under Fed.R.Evid. 803(6); or

(b) as admissions of a party-opponent, without a further showing that the declarants were "authorized" by the corporation to make the admissions, under Fed.R.Evid. 801(d)(2); or

(c) as testimony of an unavailable declarant, where the

evidence was offered in rebuttal,
and the notes and testimony were
revealed to the adverse party 9
months in advance of trial at a
deposition, but no further notice of
intention to offer the evidence was
made under Fed.R.Evid. 804(b)(5).

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TO THE UNITED STATES COURT OF APPEALS

FOR THE ELEVENTH CIRCUIT

Petitioners Donald N. and Jessica Lloyd respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eleventh Circuit in this proceeding.

OPINIONS BELOW

The District Court rendered no written opinion. The opinion of the Court of Appeals for the Eleventh Circuit is reported as **Lloyd v. Professional Realty Services, Inc.**, 734 F.2d 1428 (11th Cir.1984).

JURISDICTION

The judgment sought to be reviewed herein was rendered and entered June 22, 1984 by the Court of Appeals for the Eleventh Circuit. This Court's jurisdiction is invoked under 28 U.S.C.A. Sec. 1254(1).

CONSTITUTIONAL AND

STATUTORY PROVISIONS

Ala.Code Sec. 8-6-4 (1977)

Ala.Code Sec. 8-6-11(a)(8) (1977)

Ala.Code Sec. 8-6-11(a)(9) (1977)

Ala.Code Sec. 8-6-11(a)(11) (1977)

Ala.Code Sec. 8-6-19(a) (1977)

Ala.Code Sec. 8-6-19(b) (1977)

Ala.Code Sec. 8-6-19(f) (1977)

Ala.Code Sec. 8-6-19(g) (1977)

Ala.Code Sec. 8-6-20 (1977)

Ala.Code Sec. 8-6-30 (1977)

F.R.C.P. 31(b)

Fed.R.Evid. 804(b) (5)

Pursuant to United States Supreme Court Rule 21(f), the above are set forth verbatim in the Appendix, beginning at Page D-1.

STATEMENT OF THE CASE

The Action Below. Petitioners (the "Lloyds") filed an action for rescission of two sales of securities. Respondent Professional Realty Services, Inc. ("PRS") sold 60,000 shares of its stock to Jessica Lloyd ("Jessica") in February, 1978 for \$30,000. In August 1978 PRS sold 120,000 shares of stock to Donald N. Lloyd ("Don") for an additional \$60,000. Don paid \$40,000 by March, 1979. PRS did not issue the additional stock and, Don declined to pay the other \$20,000. The \$40,000 was not returned.

The Lloyds sought rescission for two claimed violations of the Uniform Securities Act, as enacted by the State of Alabama (the "Alabama Securities Act"). Under that Act, it is unlawful to sell securities where (inter alia):

a. the security is not registered or exempt from registration, Ala.Code Sec. 8-6-4 (1977), as to which exemption the seller has the burden of proof, Ala.Code Sec. 8-6-30 (1977); or

b. the corporation is insolvent, defined as "whenever the aggregate of its property at a fair valuation shall not be sufficient in amount to pay its debts." Ala.Code Sec. 8-6-20 (1977).

The seller of securities (here, PRS) "in violation of any provision" of the Act is liable to the buyer for the consideration paid, plus interest, costs and attorneys fees. Ala.Code Sec. 8-6-19(a) (1977). So are the seller's officers and directors (here, Ellis et al.) to the same extent as the seller, unless they can sustain a burden of proof that they did not know

and could not reasonably have known of the violations. Ala.Code Sec. 8-6-19(b) (1977).

The Facts. Ellis, et al. incorporated PRS in 1976 in Alabama. They formed it to enter into the business of marketing a national real estate brokerage franchise, "Realty World." The franchise is the same in concept as the more familiar "Century 21." The international rights to the franchise were owned by Realty World Corporation, a Delaware corporation headquartered in Virginia. PRS contracted to buy from Realty World Corporation a regional license to sell "Realty World" franchises to local real estate brokerage firms in Alabama, Tennessee and the Florida panhandle.

The parties stipulated before trial that PRS never registered any sales or offerings of its stock whatsoever, under

the Alabama Securities Act or the Federal Securities Act of 1933.¹

PRS' own financial statements indicate that it lost money every month of its operations. At trial the Lloyds introduced such of its income statements as survived its demise in 1979. A tabular summary of them appears in Appendix E.

By December 31, 1977, PRS' balance sheets indicated liabilities exceeding its assets. They so indicated at all times thereafter. The Lloyds also introduced the balance sheets at trial. Summaries of them appear in Appendix E.

¹A securities registration, state or federal, is not a perfunctory matter like the registration of, e.g., an automobile. It involves massive study and disclosure of the issuer's affairs. As a practical matter it also serves as a screening process preventing the sale of dubious investments to the public, since state (or federal) securities commissions deny effective registrations of such enterprises.

Before trial, in response to requests for admission, PRS and Ellis, et al. admitted that, at the time of both stock sales,

(1) PRS' debts exceeded the "book value" of all of its assets; and

(2) PRS' debts exceeded the "value" of its assets.

Before the stock sales, Don and Jessica were strangers to Ellis, et al. and PRS. They were neither officers, directors nor shareholders.

Shortly before the stock sale to Jessica, PRS furnished the Lloyds access to the records of the company, including these financial statements. After this sale, PRS and Ellis, et al. regularly furnished Don and Jessica with the monthly income statements and balance sheets. They did not know however that

the insolvency shown on these statements rendered sales of stock unlawful.

Neither Don nor Jessica knew, before the sale to Jessica, either that the sale was not registered or that it should have been. After Jessica's purchase, but before Don's purchase, an attorney advised them that an unregistered sale of stock by PRS was illegal under the Alabama Securities Act.

After the sale of stock to Jessica, she owned approximately 26% of PRS' stock. PRS employed Don as a salesman, and Jessica in a clerical capacity. As a condition of the sale, Don was elected a director on February 27, 1978. He served until April 14, 1978, when Jessica was elected director in his place. Don was employed as Regional Director (in effect, head salesman, though not a company officer per se) beginning May 1, 1978.

He held this position until his resignation or discharge in mid-1979. Jessica was elected nominal president of Professional Realty on August 9, 1978, which was also the date of the \$60,000.00 sale of stock to Don. Her duties remained clerical however, and Ellis, et al. remained in control of PRS.

At the time of both the sale to Jessica and the sale to Don, Ellis was a director and chairman of the board of PRS; Richards was director and president; Berry was a director; and Hooper was a director. All knew of the sales to Jessica and to Don. All knew the sales were not registered. All knew of the financial condition of PRS, as the balance sheets and income statements were furnished to them on a monthly basis.

After the sale to Jessica, the only PRS stock sales were to a Jeanne McKay

(made at the same time as Jessica's) and to Don.

In late 1979 Realty World Corporation terminated PRS' license to sell Realty World franchises, for PRS' failure to pay for the license. PRS closed its office and ceased all operations.

District Court Judgment. The district court granted a motion for a directed verdict against the Lloyds. It also granted the Lloyds' motion for a directed verdict against respondents' counter-claims.

Basis for Federal Jurisdiction. The basis for federal jurisdiction in the District Court below is diversity of citizenship and amount in controversy, under 28 USCA Sec. 1332.

REASONS RELIED ON FOR ALLOWANCE OF WRIT

**1. Knowledge of Violation of Uniform
Securities Act as Waiver of Right to
Rescind.**

The same financial statements that the Lloyds introduced at trial to prove PRS' insolvency, were made available to them by PRS before PRS sold stock to Jessica. From this, the Eleventh Circuit concluded the Lloyds had waived their right to rescind by proceeding with the stock purchase anyway:

"The Lloyds' awareness of the company's financial condition would have barred them from suing to rescind the stock sale. See Ala.Code Sec. 8-6-19(f) (1977) ("no person who has made or engaged in the performance of any contract in violation of any provision of this article or any rule or order hereunder or who has acquired any purported right under any such contract with knowledge of the facts by reason of which its making or performance was in violation, may base any action on the contract.") Appendix, p. A-8, n. 10.

This is a radical departure from the previously accepted construction of the

Act.2 By this interpretation access to information indicating insolvency, bars the buyer from rescinding for insolvency. Likewise, knowledge that stock was not registered would bar the buyer from rescinding for failure to register, and so forth.

This was indeed the law under the old state "Blue Sky Laws". Those laws, beginning with the Kansas act of 1911, generally provided for a right to rescission of a sale of securities by the buyer, if the sale was made in the

2It is also in direct conflict with an unreported case that has come to petitioners' attention, since the filing of the original version of the petition. See **Hayden v. McDonald**, ___F.2d ___ (8th Cir. 1984) (8-28-84). In that case the Eighth Circuit held squarely that the buyers' knowledge that stock was sold to him in violation of the Act, was not a waiver or bar to his recovery thereunder. The facts were if anything harsher than here. In **Hayden**, the buyers were advised by Minnesota attorneys specializing in securities law, and in some cases were Minnesota attorneys themselves.

violation of the Act. The cases under them often held that, where the buyer knew of the violation of the Act, but proceeded with the purchase anyway, he had waived his right to rescission.

But federal securities legislation has since inspired a reform of state securities laws. In 1933 Congress enacted the federal Securities Act. Under that Act it is accepted that the buyer's knowledge, that stock was sold in violation of the Act, does not waive or bar his right to a rescission under the Act.

The Uniform Securities Act, now in effect in 39 states, is a sort of spin-off from the federal Securities Act. After the federal Securities Act there arose a movement to upgrade the state Blue Sky Laws and conform them to the federal pattern. The result of this was

the promulgation, in 1956, of the Uniform Securities Act by the National Conference of Commissioners on Uniform State Laws. Professor Louis Loss of the Harvard Law School, assisted by Edward M. Cowett, drafted the Act. They specifically chose to eliminate the defense of waiver, and to impose of the type of absolute liability imposed by the federal Act. Loss discusses this as follows:

"In order to 'make the punishment fit the crime,' and consistently with the aim of furthering federal-state coordination as well as uniformity, the draftsmen closely modeled Sec. 410(a) of the Uniform Securities Act on Sec. 12 of the Securities Act of 1933. Thus, Sec. 410(a) imposes civil liability upon a person who offers or sells a security in violation ... Much of the analysis of Sec. 410(a) can accordingly be left for the subsequent discussion of Sec. 1276

* * *

76See pages 1692-1721 *infra*." Loss, **Securities Regulation** (1961), pp. 1643-1644.

The discussion referred to in footnote 76, in pertinent part, is as follows:

"The liability under Sec. 12(1) [for consideration paid, interest, etc. upon the sale of unregistered securities] is **virtually absolute**. The plaintiff need only allege and prove (1) that the defendant was a seller or ... a person in control of a seller; (2) that the mails or some means of transportation or communication in interstate commerce was used ... in the offer or sale to the particular plaintiff; (3) that the defendant failed to comply with either the registration or the prospectus requirements; (4) that the action is not barred by the statute of limitation; and (5) that adequate tender was made when the plaintiff is seeking rescission.

"The only defense then available to the defendant is to allege and prove that the particular security or transaction was exempt ... The seller's intent and knowledge of the violation ... are entirely irrelevant ... And application of the *in pari delicto* doctrine, at least on the basis solely of the buyer's knowledge of the violation, is so foreign to the purpose of the section that there is hardly a trace of it in the decisions ... " *Loss*, op. cit., pp. 1693-1694.

There is no doubt at least in the minds of the authors of the Uniform Securities Act, that a buyer's knowledge or reason to know of the violation constitutes a waiver or bar to his rescission of the sale.

What, then, of the above-quoted provisions of Sec. 410(f) of the Uniform Securities Act (Sec. 8-6-19(f) of the Alabama Act) regarding suits on such illegal contracts? The key phrase is, that knowledge of the violation prevents an action **"on the contract."** An action for rescission is not an action **"on the contract"**. It is an action in avoidance of the contract, created by and pursued under the statute. Subsection (f) has no application to it.

Loss discusses this also, to the same effect:

"Now suppose that the violator himself is suing on the contract ...

It would seem to follow a fortiori that the contract is unenforceable, at least when it is still executory on the violator's side. There would be little point in giving the seller an action on his contract only to have the buyer put things in statu quo ante by counterclaiming or bringing his own action for rescission."

* * *

"This state of affairs prompted the inclusion of the specific provision in Section 410(f) of the Uniform Securities Act ... And, at least when the violator has not yet performed his part of the contract, it is difficult to imagine a court's failure to honor the defense of illegality ..." Ibid., p. 1669.

In other words Sec. 410(f) would prevent PRS from suing Don for the additional \$20,000.00. The suit would be a pointless harassment, since Don would have a right of rescission immediately anyway by reason of the sale's having violated the Act.

The distance by which the Eleventh Circuit's interpretation of Sec. 410(f) missed the mark is graphically

illustrated by the immediately following
Sec. 410(g) of the Act (Ala.Code Sec. 8-
6-19(g)(1977)):

"Any condition, stipulation, or
provision binding any person
acquiring any security to waive
compliance with any provision of
this act or any rule or order
hereunder is void."

If an explicit written waiver of
rescission for non-compliance would be
void, how can such a waiver be inferred
from knowledge of the violations alone?

The Eleventh Circuit, despite the
history behind the Act, the comments of
its author, the provisions of its
subsection (g), and its relation to the
federal Securities Act, has reverted to
caveat emptor - exactly what the federal
and Uniform Acts seek to avoid. This
interpretation of the Uniform Securities
Act emasculates it and sets securities
regulation back, literally, eighteen
years. To avoid civil liabilities, all a

seller and its officers and directors, etc. need do is inform the buyer, in the presence of witnesses, that the sale is not being made in compliance with the Act, or even merely of the facts constituting non-compliance. The buyer would then be barred from suing for rescission, even though a written waiver would not have barred him.

Though the Uniform Securities Act is not a federal statute, cases interpreting it have been used as authority for interpreting the federal Act and vice versa. There is a significant danger that the Eleventh Circuit's view of waiver may carry over into federal law. Aside from this problem, federal courts are if anything more frequently called upon to interpret the Uniform Act than state courts, since the rescission suits typically involve violations of the

federal Act as well and are accordingly brought in federal courts.

The Uniform Securities Act is so widely in effect that its impact rivals that of federal law. It is the public's principal protection in thirty-nine states against intrastate sales of dubious securities by desperate, unscrupulous, dishonest and/or merely over-optimistic promoters, since intrastate sales are exempt under the federal Act. Actual prosecutions under it are relatively rare. As Loss indicates, the seller's and its controlling person's liabilities are meant to make the Act self-enforcing, to serve as a deterrent, to "make the punishment fit the crime." The Eleventh Circuit opens the door to easy avoidance of the Act, by letting promoters escape liability by the simple expedient of

informing the buyer of (or offering him access to information concerning) the illegality of the sale.

2. Stacking of Exemptions v. Integration of Contemporaneous Offerings

As well as evidence of offers to nine non-shareholders (*infra*), the Lloyds introduced the minutes of PRS' directors' meetings, including one in April 1978, reciting offers made to nine shareholders to sell them additional stock and/or debentures. In fact, the December 31, 1977 balance sheet reflects that \$92,747.00 had been collected from the stockholders and was carried as "notes payable - stockholders." In April 1978 a proposal was made to issue stock for these sums.

The District Court held that, in determining in whether offers were exempt from registration, offers to the nine

existing shareholders and offers to the nine others should be considered separately. I.e., an offer to nine existing shareholders would be exempt under Ala.Code Sec. 8-6-11(a)(11) (1977), and an offer to nine other persons would be exempt as made to ten or fewer under Ala.Code Sec. 8-6-11(a)(9) (1977) - even though considered together they are one non-exempt offer made to more than ten offerees, not all of whom were shareholders.

The Lloyds contend that the offers must be taken together, as one integrated offer made neither to existing shareholders only nor to ten or fewer persons. This is the accepted state of law under the federal Securities Act of 1933, upon which Professor Loss based the Uniform Securities Act.

Furthermore, the Uniform Act itself so indicates. The "small offering" exemption exempts

"Any transaction pursuant to an offer directed by the offeror to not more than ten persons, other than those designated in subdivision (a)(8) of this section in this state during any period of twelve consecutive months ..." Ala.Code Sec. 8-6-11(a)(11) (1977).

Subsection (a)(8) exempts sales to banks and other financial institutions. The drafters of the Uniform Securities Act knew how to specifically allow the small offering exemption to be stacked or cumulated with another exemption when they so chose. **Inclusio unius est exclusio alterius** - the inclusion of the right to stack the small offering exemption with the financial institutions exemption, excludes such stacking with other exemption.

Like the waiver issue, the "exemption stacking" issue affects the federal

courts and the public in thirty-nine states. It also affects the federal Securities Act. The same issue arises in determining small-offering exemptions there. It has long been thought that "exemption stacking" is not allowable, but until now there has been no case in point.³ The rule against "exemption stacking" has rested solely upon legislative history and regulations of the Securities and Exchange Commission.

3. Sufficiency of Evidence of Insolvency.

As to whether PRS was insolvent, the Lloyds bore the burden of proof.

³See also *Hayden v. McDonald*, ___F.2d___ (8th Cir. 1984) (8-28-84). While holding that the doctrine of integration could not be used to bring an otherwise prescribed sale within the statute of limitations, it acknowledged that the integration doctrine did prevent stacking of exemptions, etc.

The Eleventh Circuit stated that "the sole evidence produced by the Lloyds to show insolvency" was PRS' and Ellis, et al.'s response to the requests for admissions noted above, that the "book value" and "value" of PRS' assets were less than its liabilities.

First, this was not the only evidence. Balance sheets showing insolvency at all times from December 31, 1977 on, and income statements showing losses for all periods, were also in evidence. See Appendix E. In fact, these are the same company records by reason of access to which the Eleventh Circuit charged the Lloyds absolutely with knowledge of PRS' insolvency, and barred them from recovery. The Lloyds would have sought to rectify the overlooking of the record, at least when they were citing it, by petition for rehearing, had the Eleventh

Circuit not also made the more sweeping holding, that having seen the financial statements themselves, the Lloyds were barred from recovery anyway.

Second, the Eleventh Circuit re-interpreted Ellis, et al.'s admission that the liabilities exceeded the "value" of the assets, as also meaning "book value." This is ingenious enough never to have been urged by respondents at trial or on appeal, nor for that matter by the District Court. Rather they urged, and the District Court held below, that there was no civil liability for the violation because it had been repealed effective January 1, 1980, almost two years after the first sale to the Lloyds.

Under F.R.C.P. 36(b), "any matter admitted is conclusively established unless the court on motion permits withdrawal or amendment of the

admission." No such motion was made, presumably for the reason that Ellis, et al. meant by the admission exactly what it said. The freeing of a defendant from his admission, without a motion by him at trial or even on appeal, is such a departure from the accepted course of judicial proceedings as to warrant certiorari. It severely prejudices the party obtaining the admission when done at trial, much less on appeal. It conflicts with decisions of the other circuits interpreting Rule 36(b). **Brook Village North Associates v. General Electric Co.**, 686 F.2d 66 (1st Cir.1982).

Third, that the "value" and the "book value" admissions did not mean the same thing is evident from their proximity and different phrasing. The distinction between the two terms is well known, and

respondents knew the distinction when they made the admissions.

Finally, even if all the evidence (balance sheets, statements of income, and respondents' admissions) be construed as establishing only the proposition that the "book value" or cost of the assets was less than the liabilities, this should have been enough evidence to submit the question of insolvency to the jury. Absent persuasive evidence that the assets were worth more than cost or "book value" - and there was no such evidence - a directed verdict should have been granted the Lloyds on the issue. Normally the best evidence of the "value" of anything is price at which it changes hands between buyer and seller in a free market. *U.S. v. Davis*, 370 U.S. 65 (U.S. Sup. Ct. 1962); *Philadelphia Amusement Park Co. v. U.S.*, 126 F. Supp. 184, 130

Ct. Cl. 166 (1954). All of PRS' assets were bought since its 1976 incorporation. Depreciation was not carried until September 30, 1978, when it amounted to only some \$10,000.00. Respondents offered no appraisals or similar evidence that the assets were worth more than cost, and in fact in light of PRS' consistent and sizeable losses it would appear they were worth less. The District Court should have granted a directed verdict for the Lloyds, or in the alternative submitted the issue to the jury. Failure to do so was also a departure from accepted judicial practice warranting certiorari. The effect is not confined to the present case, as balance sheets are introduced daily in the courts as evidence of the value of a company.

**4. Directed Verdict Based Only on
Defendants' Testimony**

The Lloyds established by stipulation the unregistered sales, and, anticipating Ellis, et al.'s defense, introduced evidence as to seven more.⁴ Respondents then set about to bear the burden of proof of exemption. The exemptions claimed were, those of sales and offers to ten or fewer, and to shareholders only. Their only evidence was testimony by all of them but Ellis, that they made no offers other than to those seven and knew of no such offers made by anyone else. The Lloyds then offered rebuttal evidence which to the District Court and the Eleventh Circuit raised a jury question as to two more (non-shareholder) offerees.

⁴Aside from the offers to nine shareholders mentioned above, and aside also from minutes referring to offers to many others, of which minutes neither the district court nor the Eleventh Circuit took note.

The District Court granted the directed verdict for respondents on the issue and the Eleventh Circuit affirmed.

It described this evidence:

"The PRS defense case consisted principally of testimony by company officials that there had not been any offers in addition to the seven shown by Lloyds. During rebuttal, the Lloyds showed two more offers." Appendix, p. A-10.

"Company officials," indeed. The "company officials" consisted only of the individual defendants, excluding Ellis at that, and these were the only witnesses the respondents called. Their testimony was self-serving, incomplete both as to the absence of one of the defendants and the questions asked, and immediately controverted as well. The jury should have been entitled to weigh the credibility of the defendants' testimony, at least. Withholding the case from the jury solely by reason of testimony of

some of the defendants was a departure from acceptable judicial proceedings also warranting certiorari.

There is, again, a specifically deleterious effect upon the federal and Uniform Securities Acts. In granting and affirming the directed verdict, the District Court and the Eleventh Circuit have as good as removed the burden of proof from defendants in future Securities Act cases, state or federal. All they need do is testify that they made no offers to more than ten nor for they know of any one else who did.

5. Hearsay Evidence Exceptions

The Lloyds raise this issue primarily to reserve it, not as a reason for granting certiorari.

The Court might nevertheless undertake to clarify the question, just how under Fed.R.Evid. 804(b)(5) must a party "make

known to the adverse party ... his intention to offer" hearsay evidence of the statement of an unavailable witness? Here, nine months before trial, the Lloyds noticed and took the deposition of Ms. Bates, with Ellis, et al. present through their counsel. They were afforded copies of the deposition, including copies of the draft minutes. If this does not constitute notice, what does?

CONCLUSION

A writ of certiorari should issue to review the judgment of the Eleventh Circuit, because of the dramatic misinterpretations it has made of the Uniform Securities Act; the prevalence of the Uniform Securities Act the among various states; the frequency with which it is litigated in the federal courts; its crucial role in protecting the public

from offers of securities without registration and adequate disclosure; and the possible effect of its misinterpretation upon the federal Securities Act.

Respectfully submitted,

Robert B. Eubank

APPENDIX A

**OPINION OF UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT**

**Donald N. LLOYD and Jessica Lloyd,
Plaintiffs-Appellants, Cross-Appellees,**

v.

**PROFESSIONAL REALTY SERVICES, INC., et
al., Defendants-Appellees, Cross-
Appellants.**

No. 83-7092.

**United States Court of Appeals,
Eleventh Circuit.**

June 22, 1984

**Appeals from the United States
District Court for the Northern District
of Alabama.**

**Before KRAVITCH and ANDERSON, Circuit
Judges, and TUTTLE, Senior Circuit Judge.**

PER CURIAM:

**Appellants Donald and Jessica Lloyd
brought suit against appellees**

Professional Realty Services, Inc. and directors of the company for violations of state and federal securities laws and for fraud resulting from an attempted purchase of the company's stock. The district court granted appellees' motions for directed verdict on all counts and also granted a directed verdict for the Lloyds on a counterclaim filed by appellees. We affirm.

I.

In 1977, the Lloyds became interested in joining a real estate franchising organization. They held meetings in Alabama with representatives of Professional Realty Services, Inc. ("PRS"), a company holding an exclusive regional franchise issued by Realty World Corporation. During these meetings, the Lloyds discussed buying a local franchise in Mobile and stock in PRS. They also

met the stockholders of PRS and were given access to the financial records of the company.¹

On February 9, 1978, the Lloyds were offered 60,000 shares of PRS stock at \$.50 per share.² They accepted on the condition that Donald Lloyd would be employed as a managerial employee of PRS. Payment of \$30,000 was made in the succeeding months.³

Shortly after accepting the offer of stock, Donald Lloyd became actively

¹The company's records, as well as discussions with Realty World officials, apprised the Lloyds of PRS' poor financial condition.

²At this time, this constituted 26% of the company's outstanding stock.

³The final payment was made on April 4, 1978, and the stock certificate, issued in Jessica Lloyd's name, was delivered on May 24 of that year. Under Alabama law, a sale of securities is not complete until the actual delivery of the security. Ala.Code Sec. 7-80-301(1) (1977).

involved in the business affairs of PRS. He was elected to the company's Board of Directors, opened a PRS office in Mobile, and eventually was appointed Regional Director of the company. Jessica was similarly active. She was employed by PRS as an administrative assistant, elected to the Board of Directors, and eventually made president of the company. The couple's involvement continued until their disassociation from PRS in the Spring of 1979.

In August, 1978, a stockholders' meeting was held at which the Lloyds proposed to buy 120,000 additional shares of stock for \$60,000. Between that time and March of 1979, the Lloyds paid \$40,000, but before making the final \$20,000 payment they submitted a letter

of resignation.⁴ No additional stock was ever issued to the Lloyds.

The Lloyds filed this action against PRS and its directors (jointly referred to as PRS) in the Alabama state courts, seeking rescission of the securities sale and damages under state and federal law. Their principal claims were that PRS improperly made a sale of stock while "insolvent" under Alabama law, that the company sold stock to them in violation of state and federal registration requirements, and that the payment of \$40,000 for the never completed second stock sale was induced by fraudulent behavior on the part of PRS. PRS

⁴It is undisputed that the Lloyds submitted a letter expressing their intent to resign from their positions with PRS. There is some factual dispute about whether they were terminated by PRS before they could act on this intention. However, this factual dispute has no bearing on the legal discussion below.

counterclaimed, alleging that the Lloyds had converted company records at the time of their resignation. The suit was removed to the United States District Court for the Northern District of Alabama⁵ and, after a five-day jury trial, the court granted PRS' motions for directed verdict against the Lloyds' claims. The court also granted the Lloyds' motion for directed verdict against PRS' counterclaim. Each party contests the directed verdicts entered against it.

II.

Our discussion focuses on two principal issues, whether PRS improperly

⁵The national realty organization, Realty World, Inc., filed suit against PRS in United States District Court for the Eastern District of Virginia. Following the removal of the Alabama case to the federal district court, the two lawsuits were consolidated. All disputes between PRS and Realty World were settled before trial and are not raised in this appeal.

sold stock while insolvent and whether it sold stock in violation of state registration laws.⁶

A. Sale of Stock While Insolvent

Article 1 of the Alabama security statute sets out the general provisions regarding registration and transfer of securities. Ala.Code Sec. 8-6-1, et seq. (1977). A person who offers to sell a security in violation of any provision of this article is liable to the buyer in a

⁶We affirm without need for discussion the district court's holdings that there was insufficient evidence to create questions for the jury on the Lloyds' fraud claim or on PRS' counterclaim for conversion.

civil action rescinding the transaction.

Ala.Code Sec. 8-6-19.7

At the time of the stock sale to the Lloyds, one provision of the Article ruled that a person selling securities of an issuer known to be insolvent would be criminally liable for embezzlement.

7The statute reads in relevant part as follows:

(a) Any person who:

(1) Sells or offers to sell a security in violation of any provision of this article or of any rule or order imposed under this article ...

is liable to the person buying the security from him who may bring an action to recover the consideration paid for the security, together with interest at six percent per year from the date of payment, court costs and reasonable attorney's fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he no longer owns the security.

Ala.Code Sec. 8-6-20 (1977).⁸ The Lloyds' claim that PRS was insolvent in February, 1978, and that the sale therefore violated the statute.⁹ They further argue that this statutory violation creates an action for rescission under Sec. 8-6-19.

At the close of the Lloyds' case, the district court granted a directed verdict

⁸The statute was repealed in January, 1980, prior to the initiation of this suit. The district court correctly held that it could be applied to actions occurring during its existence. Our discussion below demonstrates, however, that no statutory violation was shown.

⁹The "insolvency" claim was not originally in the complaint. After PRS responded to a request for admission by admitting that its liabilities were in excess of the book value of its assets, the Lloyds decided to assert Sec. 8-6-20 as a ground supporting its lawsuit. The trial court initially granted a motion in limine against introduction of evidence on insolvency because the Lloyds had not notified PRS in its complaint or pretrial order that the statute would be asserted. The court later reconsidered and allowed testimony on the issue.

against them. It reasoned that Sec. 8-6-20, clearly discussing criminal liability, was not intended by the state legislature as a basis for civil liability under Sec. 8-6-19. The court read the subsequent repeal of Sec. 8-6-20 and the current regulation of embezzlement by the Alabama criminal law as support for its conclusion that the statutory civil remedy was unavailable.

While the Lloyds argue that the district court improperly interpreted the now-repealed Alabama law, we need not decide that issue. Instead, based on a close reading of the record, we conclude that the Lloyds did not put on a prima facie case of "insolvency" so as to warrant relief under the statute.

Ala.Code Sec. 8-6-20(b) defined "insolvency" as follows:

For the purpose of this section, an issuer shall be deemed insolvent whenever the aggregate of its property at a fair valuation shall not be sufficient in amount to pay its debts.

The sole evidence adduced by the Lloyds to show insolvency was PRS' affirmative response to a request for admissions served before the insolvency issue was actually in the case. The admitted requests read as follows:

1. As of January 31, 1978, the financial statement prepared internally by employees of Professional Realty Services Inc. (PRSI) showed debts totally in excess of the book value of its assets.
2. As of January 31, 1978, and at all times thereafter, the total of the debts of PRSI shown on such internally prepared financial statements exceeded the value of its assets.

We cannot conclude that these admissions, standing alone, created a jury issue on

insolvency. The term "book value" as used in the first request obviously is not equivalent to "fair valuation," the standard used by the statute. In the second request, the term "value" in context clearly refers to book value. Without additional evidence going to fair market value, there was not sufficient evidence to enable a reasonable jury to conclude that the aggregate of PRS property at a fair market value was insufficient to pay off the debts of the

company.¹⁰ See **Boeing Co. v. Shipman**,
411 F.2d 365, 374 (5th Cir.1969)
(directed verdict appropriate when
evidence is so one-sided that "reasonable

10A further support for our decision is the Lloyds' knowledge, before purchase, of PRS' poor financial condition. Realty World officials had given the purchasers such information and they had access to the PRS financial records before buying the stock. Thus, the Lloyds, experienced realtors, knew of the financial difficulties that PRS was having. Even if insolvency had been shown and civil liability was a possibility under Sec. 8-6-19, the Lloyds' awareness of the company's financial condition would have barred them from suing to rescind the stock sale. See Ala.Code Sec. 8-6-19(f) (1977) ("no person who has made or engaged in the performance of any contract in violation of any provision of this article or any rule or order hereunder or who has acquired any purported right under any such contract with knowledge of the facts by reason of which its making or performance was in violation, may base any action on the contract.")

men could not arrive at a contrary verdict").¹¹

**B. Failure to Comply With
Registration Requirements**

Ala.Code Sec. 8-6-4 (1977) renders it unlawful to offer or sell securities in Alabama unless they are "registered" in accord with other provisions of the act or subject to various statutory exemptions. It is undisputed that the PRS stock was not registered with the State Securities Commission. Therefore, the Lloyds claim that the "unlawful" sale created civil liabilities under the

¹¹In **Bonner v. City of Prichard**, 661 F.2d 1206 (11th Cir.1981) (en banc), this court adopted as binding precedent all of the decisions of the former Fifth Circuit handed down prior to the close of business on September 30, 1981. Id. at 1209.

remedial provisions contained in Sec. 8-6-19.12

PRS argues that its stock offers were exempted from registration requirements by various exceptions contained in Ala.Code Sec. 8-6-11 (1977). That section provides, *inter alia*, that registration requirements will not apply to "small offerings," i.e., offerings made to fewer than 10 people during any period of twelve consecutive months. Ala.Code Sec. 8-6-11(a)(9).

12The Lloyds also argue that PRS violated federal registration requirements. Because the complaint did not clearly state that cause of action, and because the Lloyds failed to include it in the pretrial order specifying issues to be tried, the district court refused to entertain evidence or argument on that ground. We do not find this decision to be an abuse of the broad discretion accorded to the trial judge to control pretrial procedures. *National Distillers & Chemical Co. v. Brad's Machine Products*, 666 F.2d 492, 497 (11th Cir.1982).

At trial, the Lloyds introduced evidence to show that PRS had made numerous offers of its stock prior to the February, 1978, offer to the Lloyds. At the close of the plaintiffs' case-in-chief, the trial court found that there had been sufficient proof of seven offers to allow submission to the jury, but that other purported offers were too insubstantial to be submitted. The court nevertheless denied a motion by PRS for directed verdict at that point, correctly holding that the Lloyds had met their initial burden simply by proving that PRS had sold unregistered stock.

The PRS defense case consisted principally of testimony by company officials that there had not been any offers in addition to the seven shown by the Lloyds. During rebuttal, the Lloyds showed two more offers. They also

attempted, unsuccessfully, to introduce evidence of an offer by PRS employee Norwood to "nine doctors from Stone Mountain, Georgia." The district court, ultimately counting only nine offers, found that PRS had shown its entitlement to the "small offering" exemption and thus granted a directed verdict.

In reviewing the directed verdict for PRS, we consider three aspects of the court's ruling: (1) whether the court appropriately excluded the evidence concerning the Norwood offer, (2) whether it ruled correctly that various purported offers were too weakly supported to be submitted to the jury, and (3) whether directed verdict was inappropriate because the jury, on its own, could have believed that more offers had been made.

1. **The Norwood Offer:** During their rebuttal case, the Lloyds attempted to introduce evidence that PRS employee Robert Norwood had made stock offers to "nine doctors from Stone Mountain, Georgia" sometime prior to the October 1977 meeting of the PRS board. Evidence of this offer was contained in a draft version of minutes of the October 1977 board meeting. The Lloyds sought to introduce this draft through corporate secretary Gerry Bates, or, in the alternative, have Bates testify about her recollection of Norwood's purported offers. At the time of trial, Norwood was not available to testify.

The Lloyds argued that the evidence, apparently hearsay, was admissible via three exceptions to the general proscription against such testimony. The district court found each exception

inapplicable and disallowed the testimony.

On appeal, the Lloyds reassert the reasons for which this testimony should have been admitted. They first claim that the draft minutes were "business records" admissible pursuant to Fed.R.Evid. 803(6). Although the draft minutes had been prepared by the corporate secretary, the trial court excluded them because they were not "trustworthy."¹³ The draft was marked and edited and was quite different from the final copy of the minutes which had been previously entered in evidence. The court did not abuse its discretion by

¹³Fed.R.Evid. 803(6), while setting forth the prerequisites for admission of business records, recognizes that such records should be excluded if "the source of information or the method or circumstances of preparation indicate lack of trustworthiness."

excluding the draft minutes for this reason.

The Lloyds further claim that Bates should have been allowed to testify about Norwood's statements because they were admissions by a party-opponent. Fed.R.Evid. 801(d)(2). The trial court refused to find Norwood's statements to be "admissions" of PRS unless the Lloyds could show that Norwood had some authority.¹⁴ Because the Lloyds could not show any such authority, it was appropriate to reject this asserted ground for admission of the evidence.

¹⁴Fed.R.Evid. 801(d)(2) allows the admission of a statement against a party (in this case, PRS), if it is ... "(c) a statement by a person **authorized** by [it] to make a statement concerning the subject, or (d) a statement by [its] agent or servant concerning a matter within the scope of his agency or employment, made during the existence of the relationship" The Lloyds failed to draw the critical link between Norwood's own statements and his authority, vis a vis PRS, to make them.

The Lloyds' final contention is that the testimony as to Norwood's statements was admissible under Fed.R.Evid. 804, which governs the admissibility of statements where the declarant is unavailable at the time of trial. It is undisputed that Norwood was "unavailable" as defined by that rule.

The district court refused to allow the testimony pursuant to Fed.R.Evid. 804(b)(5) because the Lloyds had not complied with the rule's procedural requirement, which reads as follows:

a statement may not be admitted under this exception unless the proponent of it makes known to the adverse party sufficiently in advance of the trial or hearing to provide the adverse party with a fair opportunity to prepare to meet it, his intention to offer the statement and the particulars of it, including the name and address of the declarant.

We accept the district court's ruling on this ground. Although both parties

had been present at a deposition of Bates nine months before trial, thus negating any possibility that her testimony would come as a surprise, the Lloyds failed to notify PRS that she would appear as a witness at trial to discuss Norwood's statements. While some appellate courts have affirmed district court findings that an adverse party's knowledge of the substance of the testimony will render formal notice unnecessary under this provision, *Piva v. Xerox Corp.*, 654 F.2d 591 (9th Cir.1981); *Furtado v. Bishop*, 604 F.2d 80 (1st Cir.1979), cert. denied, 444 U.S. 1035, 100 S.Ct. 710, 62 L.Ed.2d

672 (1980),¹⁵ these cases do not suggest that a trial court following the strict language of the rule to exclude testimony is guilty of an abuse of discretion. Because the Lloyds did not comply with the requirement here, the testimony was appropriately excluded.

¹⁵The Second Circuit has maintained that the formal notice requirements of Fed.R.Evid. 803(24) and 804(b)(5) must be strictly complied with. See, e.g., *United States v. Ruffin*, 575 F.2d 346, 358 (2d Cir.1978). While *Ruffin* has been cited with general approval by our predecessor court, *United States v. Atkins*, 618 F.2d 366, 372 (5th Cir.1980), there has been no explicit decision of this circuit which specifies how rigidly the notice provisions will be enforced. A leading commentator suggests that the rigid application of the notice requirement is at odds with the overriding goals of truth and fairness set out in Fed.R.Evid. 102. See *Weinstein's Evidence* Par. 803(24)[01] at 803-294. In affirming the district court's application of the notice requirement in this case, we do not foreclose the possibility that a liberal application may, in other cases, be acceptable under our deferential standard for reviewing district court evidentiary rulings.

2. **Offers Ruled Insufficient:** The district court considered testimony as to various offers allegedly made by PRS, including an alleged offer in April 1978 to the nine existing shareholders of the company, and found the allegations insufficient to warrant submission to a jury. We have examined the evidence on each of the purported offers and concur with the district court's rulings.

3. **Propriety of Directed Verdict:** The Lloyds claim that the jury should have received this case, even given that only nine offers had been shown. They argue that the jury could have found that other offers, not testified to at trial, may have been made so as to deprive PRS of the "small offering" exception.

In the absence of any other sufficient evidence suggesting offers by PRS, it was not error for the district court to grant

a directed verdict for the company. While nine offers were sufficiently established, evidence as to any other offers was correctly judged insufficient by the court to warrant submission to the jury. There would have been no basis for the jury to rule that more than nine offers had been made. Because there was no sufficient evidence to reasonably support a contrary decision, the directed verdict was appropriate. **Krivo Industrial Supply Co. v. National Distillers & Chemical Corp.**, 483 F.2d 1098, 1101-02 (5th Cir.1973).

4. **Conclusion:** Having examined the record, we affirm the district court's grant of directed verdict for PRS on the "small offering" exception to Alabama securities registration requirements.

III.

For the foregoing reasons, we affirm
the district court on all issues.

AFFIRMED.

APPENDIX B

DISTRICT COURT'S CONCLUSIONS OF LAW

1. Waiver Question [Transcript, pp. 689-691, 693]

"The Court would further conclude that plaintiffs Don and Jessica Lloyd could not in any event claim of violations of the Alabama securities laws' registration requirements with respect to any sale or offer or solicitation that was made after that period in late January of 1978 when the Lloyds were afforded and took advantage of the opportunity of inspecting the books.

"The Court finds that the Lloyds with actual knowledge of the contents of the books and records of the corporation on which they relied in seeking to establish a violation of the Alabama securities laws nonetheless proceeded to purchase stock in Professional Realty Services ...

"Although there are no Alabama cases directly on point, the Court believes that the doctrines of estoppel and waiver and in *pari delicto* are applicable where, as here, the party plaintiff has actual knowledge of the alleged violation of the act ...

"For the record, gentlemen, the Court would like to make explicit what was implicit in its earlier remarks. The Court believes that the sale of securities under the circumstances we have in this case was a voidable

transaction subject to the defenses that have been mentioned."

2. Exemption-Stacking
[Transcript, p. 490]

Question

The Court: "Now, are you telling me now that the offer [made to the shareholders] was made to Mrs. Lloyd as well as the other stockholders?

Mr. Eubank: "I am saying that for purposes of testing the exemptions, your Honor, yes it was. For purposes of testing the exemptions ... all contemporaneous offers have to be considered together."

The Court: "Well, I understand that contention and I reject it ... I'm rejecting your contention that the offer to the existing shareholders which was made on April 25th, 1978 was not an exempted transaction under section 8-6-11(11) ..."

3. Insolvency Question [Transcript, p. 459]

"Is there any civil liability under the securities laws now for the sale of securities by an insolvent issuer? ... I'm not aware of it, either. I will therefore hold that the legislature did

not intend to create civil liability under section 8-6-20 and I will grant nunc pro tunc the defendant's earlier motion to - in effect, to strike that claim ..."

4. Directed Verdict/Defendants' Testimony Question [Transcript, pp. 686-689]

Mr. Eubank: "The only evidence we have [from the defense], your Honor, is the testimony by the defendants that first, they themselves did not offer stock other than to seven individuals ... and that they themselves did not know of anyone who offered such stock."

* * *

The Court: [p. 689] "The Court finds that the defendants have carried their burden of proof and that under section 8-6-11(9) of the Code of Alabama of 1975, the transactions were exempt transactions."

1. The first of these is the fact that the
document is a copy of a document which
has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

2. The second of these is the fact that the
document is a copy of a document which
has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

3. The third of these is the fact that the
document is a copy of a document which
has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

4. The fourth of these is the fact that the
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has been written by a single person.

5. The fifth of these is the fact that the
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many years. It is not a document which
has been written by a single person.

6. The sixth of these is the fact that the
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has been written by a single person.

7. The seventh of these is the fact that the
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has been written by a single person.

8. The eighth of these is the fact that the
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9. The ninth of these is the fact that the
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10. The tenth of these is the fact that the
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11. The eleventh of these is the fact that the
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has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

12. The twelfth of these is the fact that the
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has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

13. The thirteenth of these is the fact that the
document is a copy of a document which
has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

14. The fourteenth of these is the fact that the
document is a copy of a document which
has been passed from hand to hand for
many years. It is not a document which
has been written by a single person.

APPENDIX C

JUDGMENT SOUGHT TO BE REVIEWED

UNITED STATES COURT OF APPEALS

FOR THE ELEVENTH CIRCUIT

NO. 83-7092

D.C. Docket No. CV80-C-0327-S

**DONALD N. LLOYD AND JESSICA LLOYD,
Plaintiffs-Appellants
Cross-Appellees**

versus

**PROFESSIONAL REALTY SERVICES, INC., et
al.**

**Defendants-Appellees,
Cross-Appellants**

**Appeals from the United States District
Court for the Northern District of
Alabama**

**Before KRAVITCH and ANDERSON, Circuit
Judges, and TUTTLE, Senior Circuit Judge**

JUDGMENT

**This cause came on to be heard on the
transcript of the record from the United
States District Court for the Northern**

District of Alabama, and was argued by counsel;

ON CONSIDERATION WHEREOF, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be and the same is hereby, AFFIRMED;

It is further ordered that plaintiffs/appellants/cross-appellees pay to defendants-appellees/cross-appellants, the costs on appeal to be taxed by the Clerk of this Court.

Entered: June 22, 1984

For the Court: Spencer D. Mercer,
Clerk

By: Myerill Pat, Jr.
Deputy Clerk

ISSUED AS MANDATE: July 19, 1984

APPENDIX D

STATUTES INVOLVED IN THE CASE

Ala.Code Sec. 8-6-4 (1977)

**"Registration of Securities -
Required; exceptions.**

"It is unlawful for any person to offer or sell any security in this state unless:

(1) It is registered under this article;

(2) The security is exempt from registration under section 8-6-10; or

(3) The transaction is exempt under section 8-6-11."

Ala.Code Secs. 8-6-11(a)(8), -(9) and -(11) (1977)

"Same - Exempt transactions.

(a) Except as hereinafter in this section expressly provided, sections 8-6-3 through 8-6-9 shall not apply to any of the following transactions:

*** * ***

(8) Any offer or sale to a bank, savings institution, credit union, trust company, insurance company or investment company as defined in the Investment Company Act of 1940,

pension or profit-sharing trust or other financial institution or institutional buyer, or to a dealer, whether the purchaser is acting for itself or in some fiduciary capacity.

(9) Any transaction pursuant to an offer directed by the offeror to not more than ten persons, other than those designated in subdivision (a)(8) of this section in this state during any period of twelve consecutive months, whether or not the offeror or any of the offerees is then present in this state if:

a. The seller reasonably believes that all the buyers are purchasing for investment; and

b. No commission or other remuneration is paid or given directly or indirectly for soliciting any prospective buyer.

* * *

(11) Any transaction pursuant to an offer to existing security holders of the issuer, including persons who at the time of the transaction are holders of convertible securities, nontransferable warrants or transferable warrants exercisable within not more than 90 days of their issuance; if

a. No commission or other remuneration, other than a standby commission, is paid or given directly or indirectly for soliciting any security holder in this state; or

b. The issuer first files a notice specifying the terms of the offer and the securities commission does not by order disallow the exemption within the next five full business days.

Ala.Code Secs. 8-6-19(a), -(b), -(f) and -(g) (1977).

"Civil liabilities of sellers, agents, etc.; remedies of purchasers.

(a) Any person who:

(1) Sells or offers to sell a security in violation of any provision of this article or of any rule or order imposed under this article or of any condition imposed under this article, or

(2) Offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, the buyer not knowing of the untruth or omission, and who does not sustain the burden of proof that he did not know and in the exercise of reasonable care could

not have known of the untruth or omission,

is liable to the person buying the security from him who may bring an action to recover the consideration paid for the security, together with interest at six percent per year from the date of payment, court costs and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he no longer owns the security. Damages are the amount that would be recoverable upon a tender less the value of the security when the buyer disposed of it and interest at six percent per year from the date of disposition.

(b) Every person who directly or indirectly controls a seller liable under subsection (a) of this section, every partner, officer or director of such a seller, every person occupying a similar status or performing similar functions, every employee of such a seller who materially aids in the sale and every broker-dealer or agent who materially aids in the sale are also liable jointly and severally with and to the same extent as the seller, unless the nonseller who is so liable sustains the burden of proof that he did not know, and in exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist.

* * *

(f) No person who has made or engaged in the performance of any contract in

violation of any provision of this article or any rule or order hereunder or who has acquired any purported right under any such contract with knowledge of the facts by reason of which its making or performance was in violation, may base any action on the contract."

(g) Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this act or any rule or order hereunder is void."

Ala.Code Sec. 8-6-20 (1977).

Sale of securities of insolvent issuer deemed embezzlement.

(a) Any officer, director, trustee, solicitor, agent or broker of or for any issuer, knowing such issuer to be insolvent, who shall sell any securities issued by such issuer, or who shall make any sale of any such securities of and for such issuer, shall be deemed guilty of embezzlement and, upon conviction thereof in any court of competent jurisdiction, shall be punished as is provided for in section 13-3-20.

(b) For the purpose of this section, an issuer shall be deemed insolvent whenever the aggregate of its property at a fair valuation shall not be sufficient in amount to pay its debts.

Ala.Code Sec. 8-6-30 (1977)

Burden of proving exemption or exception from definition.

In any proceeding under this article, the burden of proving an exemption or an exception from a definition is upon the person claiming it.

Fed.R.Evid. 801(d)(2).

DEFINITIONS

The following definitions apply under this article:

* * *

(2) Admission by party-opponent.

The statement is offered against a party and is (A) his own statement, in either his individual or a representative capacity or (B) a statement of which he has manifested his adoption of belief in its truth, or (C) a statement by a person authorized by him to make a statement concerning the subject, or (D) a statement by his agent or servant concerning a matter within the scope of his agency or employment made during the existence of the relationship, or (E) a statement by a coconspirator of a party during the course and in furtherance of the conspiracy.

Fed.R.Evid. 803(6).

HEARSAY EXCEPTIONS; AVAILABILITY OF DECLARANT IMMATERIAL

The following are not excluded by the hearsay rule, even though the declarant is available as a witness:

* * *

(6) **Records of regularly conducted activity.** A memorandum, report, record, or data compilation, in any form, of acts, events, conditions, opinions, or diagnoses, made at or near the time by, or from information transmitted by a person with knowledge, if kept in the course of a regularly conducted business activity, and if it was the regular practice of that business activity to make the memorandum, report, record, or data compilation, all as shown by the testimony of the custodian or other qualified witness, unless the source of information or the method or circumstances of preparation indicate lack of trustworthiness. The term "business" as used in this paragraph includes business, institution, association, profession, occupation, and calling of every kind, whether or not for profit.

Fed.R.Evid. 804(B)(5).

HEARSAY EXCEPTIONS; DECLARANT UNAVAILABLE

(b) **Hearsay exceptions.** The following are not excluded by the hearsay rule if the declarant is unavailable as a witness:

* * *

(5) Other exceptions. A statement not specifically covered by any of the foregoing exceptions but having equivalent circumstantial guarantees of trustworthiness, if the court determines that (A) the statement is offered as evidence of a material fact; (B) the statement is more probative on the point for which it is offered than any other evidence which the proponent can procure through reasonable efforts; and (C) the general purposes of these rules and the interests of justice will best be served by admission of the statement into evidence. However, a statement may not be admitted under this exception unless the proponent of it makes known to the adverse party sufficiently in advance of the trial or hearing to provide the adverse party with a fair opportunity to prepare to meet it, his intention to offer the statement and the particulars of it, including the name and address of the declarant.

APPENDIX E

TABULAR SUMMARIES OF PRS'

BALANCE SHEETS AND INCOME STATEMENTS

INTRODUCED BY THE LLOYDS

BALANCE SHEETS

1	Date	Assets ²	Liabilities ²	Solvency/ Insolvency ³
5	06/30/76	138,697.34	(79,505.37)	59,191.97
6	07/31/76	144,669.08	(79,219.99)	65,449.09
7	08/31/76	154,754.29	(78,129.66)	76,074.63
8	09/30/76	149,020.16	(78,679.66)	78,129.46
10	12/31/77	112,022.02	(153,916.98)	(41,894.96)
3	01/31/78	109,096.78	(155,592.56)	(46,495.78)
11	02/28/78	134,908.95	(155,051.16)	(20,142.21)
12	03/31/78	129,269.27	(154,539.01)	(25,269.74)
13	04/30/78	130,214.30	(154,475.67)	(24,261.37)
14	05/31/78	117,088.76	(152,204.38)	(35,115.62)
15	06/30/78	108,602.04	(152,148.79)	(43,546.75)
16	07/31/78	104,136.85	(149,747.25)	(45,610.40)
17	08/31/78	107,289.71	(153,733.46)	(46,443.75)
18	09/30/78	159,585.62	(198,090.02)	(38,504.40)
19	12/31/78	132,217.36	(174,751.66)	(45,234.30)
20	02/28/79	105,254.04	(187,630.66)	(82,376.62)
21	03/31/79	112,221.10	(196,329.87)	(84,108.77)
22	04/30/79	108,885.11	(191,023.27)	(82,138.16)

¹Plaintiffs' Exhibit Number, as assigned at trial.

²Figures shown on PRS' balance sheets as "total assets" and "total liabilities."

³The difference, shown as "total stockholders' equity."

INCOME STATEMENTS

4	Accounting Period	Ending Date	Income/ (Loss)⁵
5	month	06/30/76	(5,208.03)
6	month	07/31/76	(9,513.88)
7	month	08/31/76	(7,774.46)
8	month	09/30/76	(5,183.93)
8	year	09/31/76	(27,680.30)
9	month	10/31/77	(3,118.18)
10	month	12/31/77	(3,652.59)
3	month	01/31/78	(4,600.81)
11	month	02/28/78	(3,646.43)
12	month	03/31/78	(5,127.53)
13	month	04/30/78	(1,977.13)
14	month	05/31/78	(10,854.25)
15	month	06/30/78	(8,431.13)
16	month	07/31/78	(2,064.15)
17	month	08/31/78	(12,833.35)
18	year	09/30/78	(57,620.41)
19	month	12/31/78	(33,976.89)
20	month	02/28/79	(29,980.33)
21	7 mos.	04/30/79	(42,241.87)

⁴Plaintiffs' Exhibit Number, as assigned at trial.

⁵As shown on PRS' statements of income or loss.

APPENDIX F

TESTIMONY OF DEFENDANTS UPON WHICH DIRECTED VERDICT WAS GRANTED

Transcript, p. 522:

Q. Mr. Richards, between January 1st, 1977, and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, do you have knowledge of any offers or attempts to offer sales or attempted sales of stock by PRS to any other persons?

A. I do not.

Q. Mr. Richards, between January 1st, 1977, [p. 523] and September 1st, 1979, other than those persons I just named, do you have knowledge of any solicitation or attempt to solicit by PRS of offers to purchase stock of PRS?

A. I do not.

Q. Mr. Richards, between January 1st, 1977, and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, did you ever offer or attempt to offer or sell or attempt to sell stock of PRS to any person?

A. I do not.

Q. All right, sir. Between January 1st, 1977, and September 1st, 1979, other than those named persons, did you solicit or attempt to solicit an offer from anyone to buy stock of PRS?

A. No, sir, I did not.

Transcript, p. 555:

Q. Mr. Hooper, between January 1st, 1977, and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, do you have knowledge of any offers or attempts to offer, sales or attempts to sell stock by PRS to any other persons?

A. No, sir.

Q. Between January 1st, 1977 and September 1st, 1979, other than those above named persons, do you know or have any knowledge of any solicitation or attempts to solicit by PRS offers to purchase stock?

A. No, sir.

Q. Mr. Hooper, between January 1st, 1977, and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, did you offer or attempt to offer, sell or attempt to sell stock of PRS to any other person?

A. No, sir.

Q. Between January 1st, 1977, and September 1st, 1979, other than to those above named persons, did you solicit or attempt to solicit an offer to buy stock of PRS from anyone?

A. [p. 556] No, sir.

Transcript, p. 559:

Q. Mrs. Berry, between the period from January 1st, 1977 to September 1st, 1979, other than Don Lloyd, Jessica Lloyd Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, do you have knowledge of any offer or attempt to offer, sales or attempts to sell stock of PRS to any other person?

A. I do not.

Q. Between January 1st, 1977, and September 1st, 1979, other than those above named persons, do you have knowledge of any solicitation or attempts to solicit by PRS of offers to purchase stock?

A. I do not.

Q. Mrs. Berry, between January 1st, 1977, and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, did you offer or attempt to sell stock of PRS to any other person?

A. [p. 560] No, I did not.

Q. Between January 1st, 1977, and September 1st, 1979, other than those above named person, did you solicit or attempt to solicit an offer to buy stocks of PRS?

A. No, I did not.

Transcript, p. 573B:

Q. Mr. Sidwell, Between January 1st, 1977, and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, do you have knowledge of any offers or attempts to offer, sales or attempts to sell stock by PRS to any other person?

A. No.

Q. Between January 1st, 1977, and September 1st, 1979, other than to those above named persons, do you have any knowledge of any solicitation to attempts to solicit by PRS of offers to purchase stock?

A. No.

Q. Mr. Sidwell, between January 1st, 1977 and September 1st, 1979, other than Don Lloyd, Jessica Lloyd, Jean McKay, James Willis Knight, Ed Gardner, Steve Chambers and Walt Apelt, did you offer or attempt to offer, sell or attempt to sell stock of PRS to anyone?

A. No, I did not.

Q. Between January 1st, 1977, and September 1st, 1979, other than those above named persons, did you offer -- excuse me. -- did you solicit or attempt to solicit an offer to buy stock of PRS?

A. No, I did not.

DEC 7 1984

ALEXANDER L. STEVAS.

CLERK

No. 84-747

IN THE
Supreme Court Of The United States

October Term, 1984

DONALD N. LLOYD AND JESSICA LLOYD,
Petitioners,

Versus

PROFESSIONAL REALTY SERVICES, INC.,
RAIFORD ELLIS, JAMES O. RICHARDS,
LOURAINÉ D. BERRY, ALLAN W. HOOPER, JR.
AND RICHARD SIDWELL,
Respondents.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

RESPONSE TO PETITION FOR CERTIORARI

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STATEMENT OF THE CASE

Petitioners commenced this action against Respondents for violation of the registration requirements under the Securities Act of Alabama, for common law fraud, and for fraud under the Securities Act of 1933 and the Securities Exchange Act of 1934.

This action was tried in the United States District Court for the Northern District of Alabama, Southern Division, before the Honorable U. W. Clemon. At the close of Peti-

tioners' evidence, the trial court granted Respondents directed verdicts on all fraud claims and on the claim for sale of stock of an insolvent corporation, which latter claim was not raised by Petitioners in their complaint or in the pre-trial order. Upon the close of all the evidence in the case, the trial court granted Respondents a directed verdict on the non-registration claim.

Petitioners filed a timely notice of appeal to the United States Court of Appeals for the Eleventh Circuit. Following briefing and oral argument, the Eleventh Circuit affirmed the directed verdicts, holding that there was insufficient evidence to go to the jury on Petitioners' claims. The Eleventh Circuit's judgment was entered on June 22, 1984.

Respondents do not agree with Petitioners' statement of the case in its entirety; however, it would not facilitate the Court's consideration of the Petition to dispute the statements point by point at this juncture.

SUMMARY OF THE ARGUMENT

This case does not present a controlling question of law, nor a legal issue appropriate for review by certiorari under Supreme Court Rule 17.1 or otherwise. Although various alternative arguments were raised in both the district court and court of appeals, the Eleventh Circuit affirmed the directed verdicts on the basis that there was insufficient evidence to go to the jury. In reviewing the decision of the Eleventh Circuit, this Court's scope of review would be reduced to determining from the record whether Petitioners adduced substantial evidence so as to survive a motion for directed verdict. This review (a routine matter by the courts of appeal) was capably discharged by the Eleventh Circuit. Therefore, the Petition should be summarily overruled.

ARGUMENT

Respondents address in order each of the questions for review presented by Petitioners.

1. *Knowledge of Violation of Uniform Securities Act as Waiver of Right to Rescind.*

Petitioners assert that the Writ should issue because the Eleventh Circuit erred in holding that waiver and estoppel are defenses to a purchaser's action for rescission under the Securities Act of Alabama. A reading of the Eleventh Circuit's opinion, however, reveals that the court did not decide the case on the basis of waiver and estoppel. The court simply held that there was not sufficient evidence to go to the jury on Petitioners' claims.

Petitioners claimed that Respondents were liable to them for (1) selling stock of an insolvent corporation (Ala. Code § 8-6-20) and (2) selling unregistered stock (Ala. Code § 8-6-19). With respect to the first claim, the Eleventh Circuit held that the Request for Admissions and other evidence introduced by Petitioners was insufficient to make out a *prima facie* case under the statute. As to the second claim, the court held Petitioners' evidence was insufficient to go to the jury on alleged offers of stock to more than ten persons. (As to the second claim, Respondents contended that the offer or sale to Petitioners was exempted under Ala. Code § 8-6-11(a)(9).) It is clear that the Eleventh Circuit's decision is premised upon the state of the record, *i.e.*, sufficiency of the evidence. The Eleventh Circuit simply held that a reasonable jury could not find that more than nine offers had been made (the pertinent exemption being for ten or less offers or sales). The reference to waiver does not appear in a footnote; however, those remarks are noted in passing and were not central to the court's decision.

Accordingly, none of the grounds in Supreme Court Rule 17.1 are present. The opinion involves no compelling legal question, but simply the state of the record on review of a directed verdict. The Petition is due to be summarily overruled. *See, e.g., Rice v. Sioux City Memorial Park Cemetery*, 349 U.S. 70 (1955).

2. *Stacking of Exemptions v. Integration of Contemporaneous Offerings.*

Petitioners' assertion that this is a valid issue for review by certiorari is astonishing. The Eleventh Circuit's entire discussion of the alleged offer to "existing shareholders" consists of the following:

2. *Offers Rules Insufficient:* The district court considered testimony as to various offers allegedly made by PRS, including an alleged offer in April 1978 to the nine existing shareholders of the company, and found the allegations insufficient to warrant submission to a jury. *We have examined the evidence on each of the purported offers and concur with the district court's rulings.*

734 F.2d at 1434 (emphasis added).

Unquestionably the Eleventh Circuit's review was limited to a review of the evidence — not the legal question of "exemption stacking." There is no legal issue raised in the opinion and the suggestion that there is a legal issue for this Court's review is illusory, if not misleading.

3. *Sufficiency of Evidence of Insolvency.*

Again, Petitioners, in essence, ask this Court to review the sufficiency of the evidence to determine if a directed verdict was appropriate. Such review is not a ground listed in Supreme Court Rule 17.1 for certiorari and this Court, with all the demands placed upon it, should not be asked

to review the sufficiency of evidence on a motion for directed verdict. Petitioners do not even argue that a controlling question of law is involved in this ground. As an aside, Petitioners' assertion at page 27 of the Petition that Respondents did not assert the referenced contentions as to "book value" in the lower courts is a direct misstatement and it is disturbing that Petitioners would make such a statement to the Court.

Accordingly, the Writ is due to be denied.

4. *Directed Verdict Based Only on Defendants' Testimony.*

As with the preceding issue, this ground is simply a sufficiency of the evidence question and will not support issuance of the Writ.

5. *Hearsay Evidence Exceptions.*

Petitioners expressly state that they do not raise this issue as a reason for granting certiorari so further comment is unnecessary.

CONCLUSION

The Eleventh Circuit's opinion made no interpretation of the Securities Act of Alabama. There is no question of law involved which is postured for resolution by this Court. On appeal, the case was simply decided on the sufficiency of the evidence and the directed verdicts granted by the district court were correctly affirmed.

Similarly, the case involves no legal questions under the state or federal securities laws, such as to be frequently litigated in the federal courts. This case simply involves the sufficiency of the evidence in a securities case. Likewise, there are no Constitutional questions raised, nor conflicts

between the circuits, nor conflicts between the federal and state courts.

Although it would be an honor to address this Court, this particular case is not worthy of presentation to the Court and should be allowed to regain its humble place amongst the vast array of cases which are the daily labors of the lower courts.

Respectfully submitted,

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